

Welcome to *Policy Matters*, an engaging and informative monthly e-newsletter featuring expert insight and analysis on emerging relocation products, policies and services that can provide immediate benefit to your organization.

## How the Home Buyer's Tax Credit Impacts Transferees and Relocation Programs

Aimed at driving home-sales, some of the more popular programs created by the government to jump start the economy were various tax credit incentives. With the widespread success of these programs among first time and existing home-buyers, a significant number of transferees have been impacted. As a result, transferees are increasingly asking their companies to consider the financial impact their relocation will have on eligibility for these tax credit incentives.

This issue of *Policy Matters* will review the various implications that the tax credit programs may have on transferees and will address three common questions transferees are asking of companies.

### The Three Most Common Questions from Transferees:

**Question One:** If I am required to re-pay the 15 year tax credit/loan (provided prior to 2009) as a result of a relocation in which I sold my home, will the company assist me with the early payback requirement?

#### Background:

In 2008, a provision in *The Housing & Economic Recovery Act of 2008* offered qualified, first-time buyers a refundable income tax credit up to \$7,500, with the objective of stimulating the housing market. Acting more like a loan, this tax credit has to be repaid by the home owner over a 15 year period. For example, an eligible taxpayer who bought a home in 2008 and properly claimed the maximum available credit of \$7,500 must begin repaying the credit by including one-fifteenth of this amount, or \$500, as an additional tax – beginning with their 2010 return until 2025. It is this required repayment which makes the first legislation more like a loan than a pure tax credit which, if time and occupancy requirements are met, does not require repayment.

#### The Relocation Impact:

Under this legislation, if the home is sold before the 15 year period is up, the transferee will have to repay the remaining loan balance—in other words, the balance is due in full within two years after the home is sold or is no longer the principal residence. The remaining amount of credit owed is

repaid by any profit gained from the home sale. If the home-sale doesn't generate a profit, then the balance of the tax credit owed is forgiven. However, it should be noted that the IRS stipulates loss or gain based not on the purchase price of the home but rather the purchase price *less* the amount of the tax credit. For example, for a \$300,000 home the IRS would consider a gain to be any amount over \$292,500 (\$300,000 less \$7,500).

**Recommendation:**

Because this program works more like a loan than a pure tax credit, the transferee does not have a strong case in stating that they lost money. At most, they are paying back what they were "loaned" and in many cases that loan may be forgiven (in whole or in part) if the home was sold at a loss. In most instances, the amount due as a result of a relocation is less than the initial benefit received. Consequently, there is not a compelling reason for companies to provide relocation assistance to transferees in this scenario – namely, those who must repay the loan earlier than planned due to the relocation and home sale. Although the transferee may make the point that the earlier repayment resulted in a cash flow issue, at the end of the day there is not a quantifiable loss.

**Question Two:** If I have the \$8,000 or \$6,500 tax credit (post 2008) and I do not keep my home for the required three year period due to a relocation, and am therefore required to return the full tax credit – will the company reimburse me for the loss of this tax credit?

**Background:**

Following 2008, the home buyer credit was renewed as a part of the *American Recovery & Reinvestment Act of 2009*. The new version of the tax credit was increased to \$8,000 for qualified, first-time buyers. The bill also provided a tax credit up to \$6,500 for qualified move-up or repeat home buyers (existing home owners).

Terms of the 2009 home-buyer credit:

- The law defined a qualified move-up home buyer as one who has owned and resided in the same home for at least five consecutive years of the eight years prior to the purchase date.
- For married taxpayers, the law tests the homeownership history of both the home buyer and his/her spouse. Both spouses must qualify as long-time residents, with at least five years of principal residency for each.
- Repeat home buyers do not have to purchase a home that is more expensive than their previous home to qualify.

In comparison to 2008, a key difference of this tax credit program is the tax credit is not treated as a loan. As long as the residence purchased is not sold and continues to be the primary residence for a minimum of three years from the date of closing, the tax credit is not required to be repaid. However, if the home is sold before the required three years, then some or all of the tax credit is due back to the IRS. If there is a loss on the sale of the property, the pay back of the tax credit would be reduced by the amount of the loss measured against the purchase price less the tax credit. If there is a gain, then this gain must be paid back up to the original credit amount. As stated above, the IRS considers a gain to be based on the purchase price of the home *less* the amount of the credit.

**The Relocation Impact:**

In this situation, many companies are being asked by their transferees to reimburse the tax credit they have to repay. In today's housing market it may seem that not many transferees would be in a gain situation. However because of the way that the IRS calculates a gain, some transferees are

faced with repaying all or part of the tax credit. Thus, transferees point out that they are not able to meet the three year occupancy rule due solely to the relocation and if it were not for the relocation the tax credit would be permanent. They see this cost as “relocation driven” and appropriate for reimbursement.

**Recommendation:**

Each company will want to consider their own culture in deciding whether to provide assistance in this area. However, it is logical for a transferee to see this unexpected expense (the loss of the tax credit) as being directly tied to the relocation. For that reason, we believe that companies should treat these requests as reasonable. Regardless of the position taken, companies should have a well thought out basis for why they accept or deny these claims.

**Question Three:** As a result of relocation expenses/reimbursements added to my W-2, I did not qualify for all or part of the tax credit—will the company make up the difference?

**Background:**

The tax credit program does have phase-out income limitations. The full tax credit applies for single taxpayers earning up to \$125,000 and \$225,000 for married taxpayers filing a joint return. Reduced tax credits are available for some buyers with a modified adjusted gross income (MAGI) above those phase-out limits. The phase-out range for the tax credit program is \$20,000. Meaning, the reduced tax credit is available for some single taxpayers earning over \$125,000 and under \$145,000 and for certain married taxpayers earning over \$225,000 and under \$245,000. The tax credit no longer applies for single taxpayers earning over \$145,000 and married taxpayers earning over \$245,000.

For example, a married couple that has a MAGI of \$235,000 would be \$10,000 over the phase-out limit of \$225,000. To determine the partial amount of tax credit they would be eligible for, they would divide the \$10,000 of income that they are over by the phase-out range of \$20,000, which yields 0.5. When you subtract 0.5 from 1.0, the result is 0.5. They would then multiply the \$8,000 by 0.5, which produces a partial tax credit of \$4,000.

**The Relocation Impact:**

Transferees assume they met the MAGI earning limitations only to find out that since their relocation expenses, reimbursements and allowances have also gone into their W-2, they do not qualify for the tax credit. Therefore, they make the case that if they had stayed in their old location and made a home-purchase (which they were planning to do) they would have qualified for the tax credit. They would like to buy a home in the new location but cannot do so without the tax credit, and they aren't eligible for this tax credit now due to the relocation expenses being included in their W-2.

**Recommendation:**

In this case, SIRVA recommends the company not provide a tax credit “equalization-like” reimbursement based on income levels. We believe that most companies will follow their established precedent, with the majority not providing for individual circumstances based on the transferee's total income (including outside income). A majority of companies who do tax gross-up (and do a year-end true up) only consider W-2 income—they do not consider any outside income be it rent, trust or spousal income. So in effect, a transferee with such outside income will often pay more in taxes than they would have paid if not for the relocation. This should be considered by companies when deciding whether to reimburse any lost tax credit. SIRVA believes this reasoning provides sufficient basis for not reimbursing the perceived lost tax credit due to the relocation. If an exception is made, then any tax credit loss should be based solely on the employee's W-2 income.

In addition to the three common questions from transferees, the following is another tax credit consideration for companies to evaluate:

**Question Four:** To determine if there is a gain or loss on the home sale, the IRS will deduct either the \$8,000, \$7,500 or \$6,500 from the purchase price of the home depending on the benefit the transferee received. Should companies consider this fact in calculating a Loss on Sale benefit?

**Background:**

Referring back to how IRS calculates a gain (in determining if the tax credit has to be repaid when the three year rule is not met), if a home is purchased for \$300,000 and then sold for \$290,000 the IRS would not require that any of the tax credit be repaid since the home sold for less than the determined breakeven point of \$292,000 (\$300,000 minus \$8,000).

**The Relocation Impact:**

Consider a company that has a first dollar coverage Loss on Sale policy with a payment cap at \$50,000 when the purchase price is greater than the subsequent sale price of the property. In this case the transferee requests a payment of \$10,000 for Loss on Sale and does not mention that they have been allowed to keep the tax credit of \$8,000. This means that their actual loss is not \$10,000 but rather \$2,000. If the company pays them the full \$10,000 as a Loss on Sale then the transferee has pocketed an additional \$8,000 that they wouldn't have received if not for the transfer and home sale. Some companies maintain that this is undeserved transferee enrichment while others claim this is a personal tax matter and the company shouldn't know whether the tax credit was taken.

**Recommendation:**

Delving into a person's confidential tax history (required in order to justify not paying the Loss on Sale as provided for in stated policy formula) is a slippery slope. This is another reason why it is "best practice" to have a Loss on Sale program with a deductible – in this case, reducing the opportunity for the transferee to receive the best of both worlds. In determining your policy, a key question to consider is whether the number of cases in which this would occur (and the resources necessary to prove/disprove whether the credit was actually received) would justify the effort. In most cases, we have seen that it does not.

**Latest Developments**

This latest tax credit was originally scheduled to expire in the fall of 2009. Congress then extended the program through April of 2010, and recently extended the date for which a buyer could close on a new home to September 30<sup>th</sup>, 2010 as long as he/she had a purchase agreement secured on the property by the April 30<sup>th</sup>, 2010 deadline. There has been no serious activity in Congress that would indicate any further tax credit programs will be extended or offered in the near future.

**Summary**

The housing tax credit program presents a unique challenge to companies relocating employees. Due to the payback provision of the tax credit, companies asking employees who qualified for the credit to relocate may be asked to assist in repaying this credit to the IRS. The scenarios we have discussed are only a few examples, intended to give a general idea of how the tax credit might be seen in different circumstances. Companies should always consult their own tax and legal groups for specific recommendations reflecting company culture and policy.

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The foregoing is intended as general information only. SIRVA suggests that decisions as to your specific situation should be made only after full evaluation of your circumstances with your company leadership, tax and legal advisors, and HR personnel.

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